Enterprise Investment Scheme (EIS)

Created June 2015

Objective

The Enterprise Investment Scheme (EIS) is designed to help smaller higher-risk trading companies to raise finance by offering a range of tax reliefs to investors who purchase new shares in those companies.

Rules for the Company to claim relief under EIS are as follows:

1. Kind of Company

No.	Rule	Applicability of rule
i.	Must be an unquoted company at the time the shares are issued. These include: • Company listed on AIMs • Company listed on PLUS Market (now acquired by ICAP Securities & Derivative Exchange - ISDX) And excludes: • London Stock Exchange • ISDX – Listed	• Unquoted at the time of issue of shares. • Company can list subsequently as long as there were no arrangements at the time of issue of shares.
ii.	Gross assets of the company (or group) to not exceed £15 million before and £16 million after the issue of shares.	At the time of the issue of shares.
iii.	Have less than 250 full time employees (or equivalent).	At the time of issue of shares.
iv.	Must not control another company without that company being a qualifying subsidiary, i.e. the company has more than 50% of the ordinary share capital of the subsidiary and not controlled by any other person or company.	Must be met throughout a period of three years from the date of issue or three years from the date of commencement of trade whichever is later.

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No.	Rule	Applicability of rule
v.	Must not be controlled by another company (or another company and any person connected with that company). However for commercial reasons, a company can have a holding company structure if it abides by certain rules.	Must be met throughout a period of three years from the date of issue or three years from the date of commencement of trade whichever is later.
vi.	Shares can be issued only by the company carrying on the **qualifying trade** or if not the company then its parent or a subsidiary (90% subsidiary). Trade carried on in partnership will not qualify the company.	

2. Limits on raising of capital

Companies cannot raise more than £5 million in total in any 12 month period from venture capital schemes. These include- EIS, SEIS, VCTs and schemes covered by the European Commission's Guidelines on State Aid to promote Risk Capital Investments in Small and Medium-sized Enterprises.

3. Rules on employment of capital

No.	Purpose of the money being raised	Timelines for employment of funds
i.	For an existing qualifying trade.	Within two years from the date of issue of shares or commencement of trade whichever is later.
ii.	For preparing to carry on such a qualifying trade.	
iii.	For research and development intended to lead to the qualifying trade.	
iv.	To acquire shares in a 90% qualifying subsidiary and the subsidiary uses the money for i, ii, iii above.	

4. Qualifying trading activities

- The trade must be conducted on a commercial basis with a view to the realisation of profits.
- To qualify, there is no requirement for the qualifying company to be resident in the UK.
- The company must have a 'permanent establishment' in the UK.
- The trade must not be substantially (more than 20% of the activities) one of a number of excluded activities such as land dealing, dealing in financial instruments, leasing, banking, legal & accountancy services, farming, steel, coal production and others.
- Qualifying trading requirements are required to be met throughout the period of three years from the date of issue or commencement of trading activity, whichever is later.

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Rule for the Investors to claim relief under EIS are as follows:

1. Type of shares to be issued

- All shares must be fully paid up in cash on issue.
- Full-risk ordinary shares, not redeemable or carrying preferential rights to the company's assets in the event of winding up.
- Shares can have limited preferential rights to dividends, but excludes rights which allow issue of shares with
  - the right to the amount of dividend to be varied
  - the right to receive cumulative dividends
- No arrangement for protecting the investors from the normal risks as a shareholder.
- No arrangement at the time of investment for the shares to be sold at the end of the relevant period (3 years from the date of issue or commencement of trading whichever is later).
- Shares cannot be acquired using a loan acquired for that purpose.
- Shares must not be issued under 'reciprocal' arrangements.

2. EIS Relief

No.	Relief	Eligibility	Relief to be claimed	Requirement to claim
i.	Income Tax Relief	Individuals who are not 'connected' with the company.	• 30% of the cost of the shares to be set off against the individual's Income Tax liability (excludes dividend income) • Maximum tax reduction - £300,000 for any one year (maximum amount invested £1,000,000) • Relief for the year can be carried back to the preceding year (part or full)	Shares to be held for three years from the date of issue or commencement of trade, whichever is later.
ii.	Capital Gains Tax Exemption	Individuals who have received Income Tax Relief	Any gain on disposing of shares is free from Capital Gains Tax	• Claim to Income Tax Relief is made • Shares disposed of after three years from the date of issue

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No.	Relief	Eligibility	Relief to be claimed	Requirement to claim
iii.	Loss Relief	Individuals (connected and unconnected)	Any loss on disposing of shares less if any Income tax relief given, is set off against any income of the previous year	
iv.	Capital Gains Tax Deferral Relief	Individuals (connected and unconnected) and trustees of certain trusts	• Capital Gains tax arising on disposing any kind of asset can be deferred • No maximum or minimum amount of deferral	• Gain arising on disposal of any kind of asset needs to be invested in shares of an EIS qualifying company • Investment to be made within 1 year before or 3 years after the gain arose • No requirement to hold the shares for a minimum period

3. Purpose of the Scheme and other terms

- There must be no arrangement between the parties, whereby the main purpose of the arrangement is to provide a tax benefit to the investors.
- EIS relief is available only to individual investors.
- Investors who invest in a qualifying company through a partnership structure will not be eligible for tax relief.

4. Meaning of connected individual

- An individual is a connected with the company either by financial interest or by employment set out in the following table (on the next page):

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- Financial interest in the company (or in any subsidiary)
  - Control the company or holding more than 30% of the share capital, voting rights, right to assets in the event of winding up.
  - Shareholding, voting rights, right to assets in the event of winding up held by associates are to be taken into account while calculating the 30% interest.
- Connection by employment:
  - A partner, director (except business angels) or an employee of the company.

These conditions not only apply on the date of issue but throughout the period beginning 2 years before the issue of the shares and ending 3 years after the issue or 3 years after the commencement of the trade, whichever is later.

- Business Angels:
  - An investment will qualify for Income Tax Relief, if the individual (Business Angel) is a director who receives no remuneration and was not previously involved in carrying out the trade of the qualifying company at the time of issue of shares.
  - Income Tax Relief can be claimed after becoming a paid director, provided that the remuneration is reasonable and providing either:
    - those shares are issued either within the period of holding relating to the shares issued before becoming a paid director, or
    - shares are issued before the third anniversary of the date of issue of shares which qualified for relief under Seed Enterprise Investment Scheme (SEIS).
  - A connected individual is not eligible for Income tax relief on the cost of shares and capital gain tax relief on disposal of shares. The following table summarises the tax relief available depending on whether the investor is connected with the company or not:

Relief	Unconnected Investor	Connected Investor
Income Tax relief on subscription	Yes	No
Capital Gains Exemption on disposal of shares eligible for Income Tax Relief	Yes	No
Loss Relief on disposal of shares at a loss	Yes	Yes
Capital Gains Deferral	Yes	Yes

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5. Withdrawal or reduction of tax relief

Tax relief will be withdrawn if, during the 3 year period (from the date of issue of commencement of trade):

- The investor or his/her associate become connected with the company
- The company loses its qualifying status

Tax relief will be reduced or withdrawn if, during the 3 year period (from the date of issue of commencement of trade):

- Shares are disposed of (except disposal is to a spouse or civil partner)
- The investor receives 'value' from the company that includes a loan, benefit, sell of an asset by the company at less/more than market value.
- Company repays or repurchases its own share capital from any such shareholder.

6. Advance Assurance Scheme

HMRC operates an advance assurance scheme administered by the Small Company Enterprise Centre (SCEC). Under this scheme the company can present their proposed issue to SCEC to know in advance whether the scheme will qualify for a relief or not. Companies are not required to obtain such an assurance, but may do so to spot any problems before the issue or to obtain confidence from potential investors.

We hope you found this useful, but if you would like further information about the Enterprise Investment Scheme then please contact Share Plan Partners for a FREE consultation.

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